

Managing Director's Review

Review of Operations

Overview

The Group's overall business performance was steady in 2005. Broking business remained under pressure, but increased contributions from margin financing, corporate finance services and other incomes helped fill the earnings gap. Investment performance was also less satisfactory, which reflected the rather lackluster market performances in 2005. The Hang Seng Index was flat in the first half of last year, and picked up a meager 4.8% in the next six months. The index recorded a gain of 4.5% over the year. The H-shares index performed stronger, up 12.4% for the year, but was also sluggish in the first half. Retail investors generally stayed on the sidelines in a market that lacked a clear direction. Our stock brokerage business had been adversely affected, but the setback had been mitigated by our brokerage services in other financial products. Our investment banking business would have performed better if the progress of arranging the IPO for certain Chinese enterprises had not been deterred by the legal process in the PRC. During the year, we have expanded our brokerage operations in institutional business and in gold and FX trading. This explained the moderate increase in staff expenses during the year. Before a provision for doubtful debts, operating profit for 2005 was slightly higher than 2004.

Stock and futures broking

The division recorded revenue of HK\$209.3 million, down 3.3% from 2004. Securities commission income dropped 13% to HK\$139.8 million, but income from futures, options and commodities trading increased an encouraging 24.1% to HK\$68.3 million. With an expanded array of financial products, brokerage income will tend to become more diversified and stable. Our sophisticated online platform has enabled us to stretch our reach geographically, and we have been adding more overseas accounts to our sizeable client base. Our institutional sales have successfully cracked new institutional accounts, including hedge funds actively

participating in the regional markets. Our local penetration will continue to be expanded through our branch network and sales force. We have ten local branches now after the recent opening of a branch in Sai Wan and Shatin respectively, and the branch in Macau has also performed well on the back of a brisk economy. In addition to our offices in Beijing, Shanghai, Guangzhou and Shenzhen, we have been building up our presence in other cities for strategic business developments. Our independent research has been extremely useful in expanding our brokerage business as the provision of value-added services is mandatory for gaining customer patronage.

Investment banking

The division recorded revenue of HK\$67 million, up 82% from 2004. Income was mainly derived from financial advisory of HK\$18.4 million and placing and underwriting commission of HK\$48.6 million. During the year, we completed 1 IPO sponsorship assignments, 32 IPO underwriting assignments, 17 securities placements, 5 rights issue underwriting and 45 corporate advisory assignments. We have continued to focus our business on emerging Chinese enterprises which may dominate the listing pipeline, apart from larger-scale state-owned



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enterprises. We will also seek to participate in the underwriting for the IPOs of sizeable state-owned enterprises though the mandates for which are scarcely accessible to local houses. Besides, we will continue to be active in providing financial advisory services for local enterprises, with our strong connection and knowledge in the local business community.

Securities financing and money lending

The business is supplementary to our brokerage and other financial services. The division generated HK\$87.1 million in revenue, up 6.2% from 2004. Higher interest rates and a sluggish stock market had some negative impact on the demand for financing services last year. We have been able to get financing from the banks at better credit terms, thereby improving our interest spreads in a rising interest rate environment. The provision for doubtful debts made last year related to an individual case that brought forward few years ago when the local economy was still in the doldrums. We see the charge as a non-recurrent item. Advances to customers rose to HK\$902.4 million as at the end of 2005, up 14.4% over the year.

Other investment services and activities

We see excellent growth potential in asset management and wealth management businesses, and have continued to build up our capability in these areas. Apart from the CM Tai Fook China Investment Fund launched in September 2003, we have set up another China investment fund, namely Tai Fook Aizawa Attractive Dividend Yield Chinese Stock Fund, in October 2005 to tap Japanese investors. We have optimised the employment of our financial resources by engaging in proprietary trading activity, which covers trading in securities, futures, options, FX and other commodities. We have adequate professionalism and risk management to ensure that sound investment returns could be achieved with calculated risks. Trading securities amounted to HK\$94 million as at the end of 2005, while we also held HK\$74.2 million worth of securities for longer-term investment.

Future Plans

Our future growth will be supported by our well established business and organisation framework, which has clearly identified the key earnings drivers and the necessary infrastructure and management are in place. We have insisted on the commitment in staff development and IT capability in the past, and will remain so in the future. However, I envisage that the Group will pursue a more aggressive strategy in business development ahead, which will leverage our manpower and fixed investments more effectively and the result will be enhanced returns both to our staff and shareholders.

Our brokerage, investment banking and asset management businesses will target both organic growth and drivers from strategic partnership. The opening China market is perceived to be offering immense opportunities for us to significantly expand our client base and financial services longer term. On the brokerage side, we are planning for a licensed operation in futures trading in the China market through an acquisition in Shanghai. Our asset management business has already set up good partnerships with major China financial institutions and has successfully launched investment funds focusing on China securities. An Asian IPO fund has been closed recently with an initial fund size of US\$28 million. Our experience and flexibility give us an edge in partnering with overseas institutional investors wishing to make their first move into the China market. We expect to reach an important alliance in the near future. Our investment banking business will become even stronger in respect of deal sourcing, fund raising and distribution as our client base and placing capability are further enhanced.

I am confident that satisfactory operating results will be achieved for the current year. However, the longer term growth of the Group will be dependent on the efforts and dedication of our staff, under the leadership of our visionary management. I would like to express my gratitude to all of them on this annual occasion, and the continued support from our stakeholders and shareholders is appreciated.

WONG Shiu Hoi, Peter

Managing Director

Hong Kong, 10 April 2006